

**Drinking Water State
Revolving Fund Program**

Supplemental Guidance



February, 2001

**Region III
U.S. Environmental Protection Agency
Philadelphia**

DISCLAIMER

The statements in this document are intended solely as guidance. This document is not intended, nor can it be relied upon, to create any rights enforceable by any party in litigation with the United States. EPA may decide to follow the guidance provided in this document, or to act at variance with the guidance based on its analysis of the specific facts presented.

TABLE OF CONTENTS

INTRODUCTION	2
PROJECT PRIORITY LIST	2
Contents of Project Priority List	2
Funding of Projects and Priority Rankings	3
Bypass Provisions	3
Management of Priority Lists	4
Public Review of Changes to the Project Priority List	5
INTENDED USE PLAN	7
Development and Submission of the Intended Use Plan	7
Short-Term and Long-Term Goals Included in the IUP	7
Inclusion of Project Priority System and Bypass Procedures in the IUP	9
Funds to be Included in the IUP	9
Criteria and Methods Used to Distribute Funds	10
Description of the Use of Funds for Set-Aside Activities in the IUP	10
Public Review and Comment on the IUP	11
EPA Approval of the PPL/IUP	12
GRANT APPLICATION REQUIREMENTS	12
Annual Attorney General Certification	12
Contents of Set-Aside Workplans	13
Budget Detail on the Set-Aside Activities	14
1:1 Match Requirement Under the 10% Set-Aside	14
PROGRAM MANAGEMENT	15
Compliance with the Binding Commitment Requirement	15
Timing of Submission of Application to Region III and its Impact on ACH Payments	15
Reporting	16
APPENDICES	17
CAPACITY DEVELOPMENT STRATEGY FOR EXISTING SYSTEMS	17
CAPACITY DEVELOPMENT AUTHORITY (NEW SYSTEMS)	20
OPERATOR CERTIFICATION PROGRAM: POTENTIAL WITHHOLDING	22
E APPLICATION MATERIALS	23

INTRODUCTION

The Drinking Water State Revolving Fund (DWSRF) was authorized by the Safe Drinking Water Act (SDWA) Amendments of 1996. This Regional guidance supplements the DWSRF Program Guidelines (February 1997), the DWSRF Interim Final Rule (August 2000), and the sets of Questions and Answers distributed by EPA Headquarters. This Regional guidance formalizes policies that were developed and informally communicated to states as they implemented their DWSRF programs. As such, some of the policies outlined in this document have been applied to DWSRF grants already awarded. The policies contained in this document apply to all DWSRF grants awarded after October 1, 2000.

The DWSRF Interim Final Rule provides the legal basis for most of the requirements noted in this guidance document. Specific sections of the rule are cited, as appropriate, throughout this document. This guidance document does not establish new program requirements.

The key component of a state's DWSRF program is its Intended Use Plan (IUP). Most of this guidance document relates to the contents of the IUP, although portions relate to the capitalization grant in general and the overall management of the DWSRF program. Region III will issue additional guidance on the development of set-aside workplans and reporting of set-aside activities.

PROJECT PRIORITY LIST

Contents of Project Priority List

A state's Project Priority List (PPL) is the portion of the IUP that identifies the projects expected to receive loans for drinking water infrastructure improvements. The IUP must identify projects on a fundable list and projects on a comprehensive list [section 35.3555(c)(2)(i)]. The fundable portion of the list identifies projects which the state expects to receive DWSRF loans in the current year. The comprehensive list also includes the next most highly ranked projects, which will likely be funded in future years or in the current year if one or more of the projects on the fundable portion of the list are bypassed. These two lists may be combined into one list, as long as there is a clear indication of which projects on the single list are expected to receive funding in that year.

The fundable list of projects must have the following information provided for each project:

- The name of the public water system,
- The priority assigned to the project,

- A description of the project,
- The total cost of the project and the expected terms of financial assistance based on the best information available at the time the IUP is developed, and
- The population of the system's service area at the time of the loan application.

Projects on the comprehensive list also must be ranked and assigned a priority. If sufficient information is not available to rank the project at the time the comprehensive list is developed, the project may not be included. In addition, the comprehensive list must also include, to the extent known, the expected funding schedule for each project.

Funding of Projects and Priority Rankings

Section 1452(b) of SDWA requires state DWSRF programs to fund projects in priority order, to the maximum extent practicable. The projects submitted in a state's IUP are listed in priority order at the time of the IUP preparation. Although the state is required to fund projects in priority order, this does not mean the state must execute loans in rank order.

Section 1452(a)(2) of SDWA requires that a state use at least 15% of all funds credited to the Fund account (i.e., infrastructure project loan account) to provide loan assistance to small systems to the extent practicable. In addition, section 1452(d) of SDWA allows the state to provide loan subsidies to disadvantaged communities up to, but not exceeding, 30% of the amount of the capitalization grant for each year.

Bypass Provisions

The DWSRF rule allows a state to bypass a project on the fundable portion of the PPL if the state's bypass procedures clearly identify the conditions under which a project may be bypassed and the method for identifying which projects would receive funding. [Section 35.3555(c)(2)(ii)]. The state may include a mechanism in its bypass provisions to ensure that the small systems target is met.

If the state chooses to bypass a project for reasons allowed in its bypass provisions, the state must consider funding the highest ranked project on the comprehensive list that is ready to proceed. Each project must be considered sequentially. It is not acceptable for a state to choose to fund a project further down on the comprehensive list unless all intermediate projects have been considered, including being evaluated for "readiness to proceed" as defined by the state.

States' active management of the fundable portion of the PPL and provision of technical assistance to systems that are not ready to proceed should help reduce

delays. States may also choose to establish a time frame in which a project should be ready to proceed. For example, a state may choose to define a project “ready to proceed” if it can enter into a loan agreement within 12 months of IUP approval by EPA. If this cannot be done, the state may wish to consider bypassing the project. This would better ensure that the state will commit and expend funds as efficiently as possible and in an expeditious and timely manner.

States are required to provide information on project bypasses in their biennial reports. EPA will review bypasses during its annual reviews of state programs. Region III suggests that the states periodically update the Region III DWSRF Coordinator with information on project bypasses within the fundable portion of the PPL and/or the comprehensive list, consistent with the state’s bypass provisions. In each instance, the state would describe why it was not practicable to fund a project or projects that were ranked higher than the funded project and explain what projects were added to the fundable portion of the PPL.

The only instance in which a state would fund a project that is not on its current comprehensive list is in an emergency, provided that the IUP defines what conditions constitute an emergency. If a state bypasses a number of projects for various reasons (e.g., projects not ready to proceed, the addition of emergency projects), it should consider a new solicitation to ensure that (1) all projects are considered, (2) the required public review occurs, and (3) the most highly-ranked projects are funded. Region III encourages states to include projects on the fundable list only if they are likely to actually apply for funding within that year.

Management of Priority Lists

It is normal for infrastructure project cost estimates in the IUP to be higher or lower than actual construction bids and actual closed loan amounts. States should note in the IUP that the amounts shown are estimates and could change. In particular, for communities on the lower portion of the project funding list, the state should be careful to indicate that funding is not ensured. If there is a significant increase in project costs (perhaps +25%), the state could consider providing the balance of the needed funds in a subsequent IUP (phase funding the project). A change between the original cost estimate and the actual costs does not require public notification.

If monies become available for projects below the fundable line due to projects being withdrawn and/or bids coming in lower than originally estimated, the state has three options:

- (1) The state could consider projects below the funding line on the current comprehensive list;
- (2) The state could solicit for a new round of projects with that money; or
- (3) A combination of (1) and (2).

Option 2 is acceptable because the law requires that the highest priority projects in terms of addressing public health and compliance with SDWA be funded.

There may be instances when the state considers all projects on the current comprehensive list and determines that no projects are available at that time for funding (e.g., not ready to proceed, found assistance elsewhere). The state may undertake additional solicitation as suggested above or it may include these funds in the next IUP and identify them as prior year uncommitted funds. These monies, plus other available funds, would be used to fund projects on the next funding list.

Public Review of Changes to the Project Priority List

The DWSRF rule stipulates that the state seek public review and comment on its PPL [section 35.3555(c)(2)]. The project list may be amended without further public review under provisions established in the IUP, so long as the project(s) which have may been added were previously identified through the public participation process.

States are encouraged to keep the fundable portion of the PPL current through periodic updates. Changes may be minor or substantive. Minor changes to the fundable portion of the PPL (e.g., to update project costs and to revise target dates) do not require additional public notification or involvement.

When the state makes substantive changes to the fundable portion of the PPL, EPA suggests that the amended fundable portion of the PPL undergo a process of soliciting public review and comment and that it be submitted to Region III for acceptance. The Region accepts the state's determination unless the Region advises the state within 30 days of receipt of the amended fundable portion of the PPL.

The following are examples of changes to the fundable portion of the PPL that require public review:

- The addition of a project or projects to the fundable portion of the PPL that have not undergone public review as part of the current PPL;
- A change in the scope of proposed projects to the extent that priority rankings change; and
- The addition of new projects to the PPL that affect the relative position of projects on the funding list.

The following two examples, however, are instances in which a project could be added to the fundable portion of the PPL without public review:

- Emergency project(s), if provided for in state procedures and
- Project(s) on a prior year funding list bypassed for a particular reason, as allowed under the state's bypass provisions.

The state will decide how public comment will be solicited, either through a formal public review process or through public notification, after considering the nature of the change, the potential for controversy, and other relevant factors. EPA suggests that at a minimum, the state:

- Provide notice of the change in a manner which is likely to reach the parties who are affected;
- Explain the change and its effect, particularly if the change is associated with imminent selection for funding; and
- Provide a forum which permits questions to be raised and answered.

When the amended fundable portion of the PPL is submitted to Region III, the state should explain:

- The nature of the changes;
- How the affected drinking water systems were notified of the changes and how comments were solicited;
- What comments were received regarding the changes; and
- The state's determination that the degree of notification was commensurate with the effect of the changes.

The state's determination will be accepted unless Region III advises otherwise within 30 days of receipt of the amended fundable portion of the PPL.

INTENDED USE PLAN

Development and Submission of the Intended Use Plan

The state must develop an IUP annually as long as the Fund account, as defined by the DWSRF rule, and/or set-aside account funds remain in operation [section 35.3555(a)]. The state must submit an IUP even if it does not intend to submit an application for a capitalization grant during that year.

The IUP identifies how the state intends to distribute the grant funds among the set-aside account(s) and the Fund and includes the list of drinking water infrastructure projects expected to be funded. Section 35.3555(b) of the DWSRF rule allows a state to develop the IUP in a two-part process so the state may submit a capitalization grant application for a portion of the funds before it completes all of the specific funding decisions. For example, if a state has not decided if and how it will use the set-aside funds, the state may issue one IUP document when infrastructure projects are identified for funding and another IUP document when the state has made choices regarding its use of the set-aside funds.

The submission of a combined IUP describing the use of all the funds is appropriate if there is sufficient detail (in particular on the use of the set-aside funds) and the state has not made significant changes to the IUP after public review.

Region III has seen some cases in which a state has applied for project funds and included information about set-asides even though it was not applying for the set-aside funds at that time. By the time the state applied for the set-aside funds, the purpose of the funds (as outlined in workplans) was significantly different from what had been in the IUP. Region III suggests that states develop an IUP for the fiscal year and include the funds that will be applied for in that year. For example, if a state applies for the FY 2000 set-asides a year after it received its FY 2000 project funds, an FY 2001 IUP would describe the use of the FY 2000 set-aside funds and the FY 2001 project funds for which the state is applying.

Short-Term and Long-Term Goals Included in the IUP

The IUP must describe the short-term goals of the DWSRF program, including how the capitalization grant funds will be used to ensure compliance with the SDWA public health goals [section 35.3555(c)(5) of the rule]. In addition, the IUP must describe the objectives of the DWSRF program over the long-term, and how the state expects to achieve these objectives.

Development of meaningful goals should reflect the strategic direction of the state's DWSRF program. Further, states should use program goals as a framework for funding decisions and program management. To be useful, goals should be specific. In

addition, goals should “push” the program to an achievable “higher level.” Goal statements should not be generic. They should reflect current thought and, as appropriate, should change from year to year.

The state should include both short-term (a year or two) and long-term goals. The discussion of goals should include a description of how projects and activities to be supported by the DWSRF relate to those goals. Such goals should reflect public health, financial management, and fiscal health of the Fund. In this regard, goals should not be merely informational processes, policy statements, procedures, or desires. Instead, to the extent possible, goals should be quantifiable – goals whose accomplishments can be measured. Measurable goals might include things such as the number of systems brought back into compliance, the number of systems receiving loans which have initiated operations, or the number of drinking water systems covered by source water protection programs. States could also reflect the accountability requirements of State/EPA Performance Agreements and the EPA measures under the Government Performance Results Act.

An example of a long-term goal that meets the above-mentioned criteria would be “Maintain the long-term financial integrity of the DWSRF by judicious use and management of its assets and by realizing an adequate rate of return.” A similar long-term goal that does not fully meet the criteria would be “Effectively manage a self-sustaining program to facilitate compliance and maintain the DWSRF in perpetuity.”

For the set-aside activities, there should be a brief discussion of the relationship between the DWSRF program and other drinking water activities in the state (e.g., source water protection, capacity development, operator certification, technical assistance to small systems).

Goals should also give a description of how the DWSRF will assist communities to ensure protection of public health and compliance with the SDWA. If applicable, the goals should reflect relationships with other state agencies, affiliated water associations, and local water suppliers to ensure that all related organizations are working together to meet mutual goals (e.g., National Rural Water Association providing technical assistance to small systems; local officials ensuring public confidence in drinking water, etc.).

Financial goals should be defined in terms of meeting specific needs which are stated in terms of dollars. Goals should discuss the extent to which the DWSRF will be operated alone or in combination with other state and Federal financial assistance programs.

DWSRF program managers should look for opportunities to develop the goals in an inclusive, participatory process. Region III suggests that the goals process include staff from other state and local departments and agencies [e.g., Public Water System Supervision (PWSS) program, local water associations], as well as the interested public.

As appropriate, such goals development processes could be combined with broader environmental goals identification processes.

In their biennial reports, states should assess progress made in achieving the goals and objectives described in the IUP. The states should also describe how the attained short-term goals have worked toward achieving long-term goals.

Inclusion of Project Priority System and Bypass Procedures in the IUP

States need to annually include in their IUPs a description of their project priority systems (PPS) and their bypass procedures so that the public and other agencies understand clearly what factors go into each and under what conditions changes may occur [sections 35.3555(c)(1) and (c)(2)(ii)].

States that provide loans under section 1452(k) of SDWA for land acquisition or conservation easements, voluntary incentive-based source water protection measures, and source water petitions need to annually include a description of the priority-setting processes used to determine how recipients will be selected and how funds will be distributed among them [section 35.3555(c)(6)(ii)]. While states must include the priority-setting process/system in their IUPs so that the public can understand the program, they can indicate that they are not soliciting comments on the system if they are not intending to change it.

Funds to be Included in the IUP

The annual IUP must describe how the state will use available funds in the coming year [section 35.3555(c)(4)]. This includes a running total of all available funds, such as the following:

- New DWSRF capitalization grant money;
- New state match money;
- Uncommitted prior year DWSRF grant money that will be carried over to the coming year;
- Prior year uncommitted state match money;
- Repayments;
- Interest earnings;
- Total dollar amount in fee accounts;
- Net proceeds of bond issues (i.e., leveraging);
- Funds transferred from CWSRF; and
- Total dollar amount in set-aside accounts, including the amount of funds or authority reserved.

This “snapshot” of available funds should be taken on a date that is specified in the IUP.

In the early years of the program, the primary source of funding has been DWSRF capitalization grants and required state match. States have generally developed IUPs in coordination with their capitalization grant applications. However, other sources of funds become available through repayments, interest earnings, and proceeds from leveraging which will need to be included in the IUP.

Criteria and Methods Used to Distribute Funds

In their IUPs, states should specify the criteria and methods that will be used to distribute funds. This discussion should include the rationale for providing different types of assistance and terms and the methods used to determine the market rate, interest rates, and fees. These items are discussed in greater detail in the DWSRF rule [section 35.3555(c)(3)]. In addition, states should use cash flow projections to support how they intend to meet their funding needs and to show the potential effects of their policies (e.g., the fiscal impact of very low interest rates) on the long-term health of the Fund.

Description of the Use of Funds for Set-Aside Activities in the IUP

Congress has authorized states to use up to 31% of each DWSRF capitalization grant to help ensure the integrity of drinking water systems and to protect source waters for drinking water. If a state chooses to “set-aside” a portion of its DWSRF allotment to support these activities, it must describe in the annual IUP how it plans to use these funds [section 35.3555(c)(6)(i)]. While much of a state’s set-aside activities may remain unchanged from one year to the next as programs are initiated and implemented, the states still need to clearly articulate specific activities. The level of detail in the IUP will be significantly less than the detail described in the set-aside workplan submitted with the grant application. To ensure that the public and other interested parties clearly understand the intended use of these funds, Region III suggests that the following information be included in the IUP:

- A statement regarding the percentage and dollar amount the state is electing to use for set-asides in the aggregate and
- An outline of the total amount in dollars and percentage of funds that will be used under each set-aside category and a general description of:
(1) how the set-aside funds will be used by category/sub-category, (2) the general schedule for their use, and (3) expected accomplishments.

The description in the IUP of the use of the set-aside funds should not merely list the allowable activities to be funded under each of the categories. Rather, the IUP should specifically identify the state’s planned use of the set-aside funds (e.g., under the 10% set-aside the state has chosen to use all of the funds to support the administration of the PWSS program). If the state is interested in submitting one IUP describing the

use of all funds, but can only describe in general the use of the set-aside funds in the IUP, the state should amend the IUP later to describe how it will use the set-aside funds for which it is applying. The amended IUP would undergo public review and comment. In many cases, the state might find that it wants to ensure review of the set-aside details by different groups from those who review the initial IUP containing infrastructure project information.

Public Review and Comment on the IUP

The public must have an opportunity to review and comment on the IUP in its entirety, even in years in which the state is not applying for a DWSRF capitalization grant [sections 35.3555(a) and (b)]. For an IUP that contains both the projects and set-asides, one opportunity for public review is sufficient, if no significant changes are made following public review. Examples of cases in which one opportunity for public review is sufficient include the following:

- No change in the scope, objectives, or work to be accomplished under any of the set-aside categories;
- No change in the project priority ranking system; or
- No change in the state's bypass provisions.

However, if the final IUP submitted with the application differs significantly from the version that was made available for public comment and the changes are not as a result of comments received during the public review process, it may be necessary for the IUP to undergo additional public review. If the state has not yet decided how it will use a portion of its funds, it should provide two opportunities for public review and comment -- one for the project portion and another for the set-asides portion.

The IUP that the state submits to EPA must include documentation that the state provided an opportunity for public review and comment on the IUP. Public review and comment should occur before the state submits the final IUP to EPA. A state may wish to provide Region III a draft IUP, either prior to or concurrent with public review. Along with the final IUP, the state should submit a summary of its procedures for public review and comment and the results of that process (i.e., a summary of comments received and responses to the comments).

Note that the set-aside workplan need not be made available for public review. At its discretion, the state may wish to obtain input from the public regarding its set-aside activities. As noted above, however, the IUP must include an identification of funding to be provided for set-aside activities and at least a general outline of objectives and activities to be undertaken.

EPA Approval of the PPL/IUP

In most cases, a state submits its IUP (including the fundable portion of the PPL) to EPA with its DWSRF capitalization grant application. In these instances, Region III will not send a separate letter to a state approving its IUP. Rather, Region III will demonstrate IUP approval by awarding a capitalization grant. If the state submits its PPL or IUP prior to a complete capitalization grant application, Region III will send a separate PPL/IUP acceptance letter to the state. EPA's goal is to award a capitalization grant or accept the state's IUP within 90 days of receipt of a final grant application or IUP.

GRANT APPLICATION REQUIREMENTS

Annual Attorney General Certification

States are required to submit an Attorney General's (AG's) certification annually with their capitalization grant applications [section 35.3545(d)]. The AG must certify that:

- The authority establishing the DWSRF program and the powers it confers are consistent with state law;
- The state may legally bind itself to the terms of the capitalization grant agreement; and
- An agency of the state is authorized to enter into capitalization grant agreements with EPA, accept capitalization grant awards made under section 1452 of SDWA, and otherwise manage the Fund in accordance with the requirements and objectives of SDWA and the DWSRF Guidelines and rule.

In addition, the state must agree to demonstrate how it complies with the requirements of capacity development and operator certification provisions to avoid withholding of funds pursuant to the SDWA. (See the Appendix for additional information) The state's annual AG certification is an appropriate place to demonstrate this compliance. The initial operator certification and capacity development submittals must include AG certifications. In subsequent years, the state needs to include an AG certification with respect to capacity development and operator certification only if there have been pertinent changes to applicable state statutes or regulations. If applicable, the program manager may want to request the AG certification for all programs at the same time to expedite processing.

Contents of Set-Aside Workplans

Note: EPA Region III is developing separate guidance on set-aside workplans and reporting. Those documents will describe in greater detail the set-aside workplan requirements.

When DWSRF funds are used to support set-asides activities, the state and EPA must negotiate a workplan indicating how funds will be spent. At a minimum, the workplan must include the following information for each of the activities under the set-aside categories [section 35.3540 (c)(3)]:

- The annual funding amount in dollars and as a percentage of the state allotment or capitalization grant;
- The projected number of staff and/or grantees/contractors needed for implementing each activity;
- The goals and objectives, outputs, and deliverables for each activity;
- A schedule for completing each activity;
- Identification and responsibilities of the agencies involved in implementing each activity, including activities proposed to be conducted by a third party; and
- A description of the evaluation process to assess the work funded for each activity.

The set-aside workplan must explain and display clearly what activities are being funded with the new DWSRF capitalization grant, as an increment over and above previous capitalization grants. The semi-annual progress reports on the set-asides would describe the funds that have already been expended or obligated and the activities already completed from previous multi-year workplans. This information is essential so that EPA, Congress, and the public can easily and clearly understand how previously appropriated funds have been used and what additional work will be completed. More importantly, in each workplan, as appropriate, the state should highlight new initiatives and major program changes.

Budget Detail on the Set-Aside Activities

There needs to be a clear connection between the description of the use of the set-aside funds and the budget figures on the budget detail pages in the capitalization grant application. The IUP needs to clearly show how much money the state is requesting for each of the set-asides and each of the subactivities under each of the set-asides. There needs to be budget detail presented for each subactivity as well as for each set-aside in total. The budget pages need to be accurate and must equal the amounts requested for each set-aside and the totals for which the state is applying. The budget summary information should readily track with the detail and organization of the set-aside workplan.

1:1 Match Requirement Under the 10% Set-Aside (State Program Management)

Section 1452(g)(2) of SDWA requires that states contribute a dollar-for-dollar match for the state program management set-aside. The law also allows some of this

match to come from a state's match and overmatch under the FY 1993 PWSS grant. However, at least one-half of the state's match funds must be in addition to the amount that the state expended for the PWSS program in FY 1993. In other words, one-half of the match must be from "current fiscal year" PWSS expenditures (i.e., PWSS grant overmatch and other approved state expenditures). The statute does not define "current fiscal year." The term "current fiscal year" could mean (1) the fiscal year of the grant allocation, (2) the fiscal year in which a state is applying for DWSRF funds, or (3) the year in which the funds will be expended. The state may choose one of these options, so long as it does not count the same dollars twice.

If a state distributes funds over a multi-year workplan, it may provide the match up-front at the time of the grant award or at the time expenditures are made pursuant to the set-aside workplan. It is essential, however, that the state not double-count the dollars it is using to meet the match requirement. For example, if a state uses its FY 2000 PWSS overmatch as credit for meeting the match for FY 1999 allotted DWSRF funds, it may not then use its FY 2000 PWSS overmatch as credit for meeting the match requirement for FY 2000 allotted DWSRF funds.

In addition, states may not reserve overmatch credit. If a state leaves funds unspecified and deposits them into the infrastructure Fund and reclaims them some years later to fund 10% set-aside activities, the state cannot go back and take credit for any overmatch it had provided in prior years. The required match would have to come from the "current" year (or years) covering the workplan.

PROGRAM MANAGEMENT

Compliance with the Binding Commitment Requirement

Within one year after the receipt of each grant payment, a state must enter into binding commitments (BCs) with assistance recipients in an amount equal to each grant payment and accompanying state match [section 35.3550(e)].

Occasionally, projects are unable to proceed for unforeseen reasons. If possible, the state could modify project schedules so that other projects may be counted toward the BC requirement. It is important that the state closely monitor project status and provide assistance as needed to maintain schedules.

If the state will not be able to meet the BC requirement, it may wish to revise its Automated Clearinghouse (ACH) schedule, to the extent allowable. The state is able to make revisions to its ACH schedule to delay payments that have not yet occurred. Consequently, a state can modify the time frame in which it must enter into BCs. Payments that have already been made cannot be rescinded. Although revisions to the schedule are allowed, all payments (except FY 1997 funds) must be made by the earlier of 8 quarters from the date of the award or 12 quarters from the date of the allotment [section 35.3560(b)]. To amend its ACH schedule, the state will need to formally request an amendment to the applicable assistance agreement by submitting a revised payment schedule to Region III's Grants and Audit Management Branch (GAMB). The state should provide Region III with as much notice as possible should it choose to amend its schedule (preferably at least 60 days prior to the next payment).

The DWSRF rule includes provisions on compliance assurance (section 35.3585). EPA is instructed to issue a notice of non-compliance if appropriate. Failure to meet the binding commitment requirement would be one instance when EPA may issue a notice of noncompliance. Region III intends to issue a policy on the issuance of noncompliance letters as well as related program compliance notifications and actions.

Timing of Submission of Application to Region III and its Impact on ACH Payments

When applying for capitalization grants, states should keep in mind the requirement that all ACH payments must be made by the earlier of eight quarters from the date of a capitalization grant award or 12 quarters from the date of allotment. This requirement could cause problems for a state if an award is made near the end of a quarter, since the quarter in which the award is made counts as the first quarter. For example, with respect to the ACH payment schedule, an award made on September 30 is the same as an award made on July 1. Therefore, states that receive awards late in a quarter effectively lose one quarter in which to receive ACH payments (and thus to complete BCs). This will not be a problem if the state is expecting to make BCs fairly quickly. However, in a situation in which the state is expecting that there will be many

BCs in the last few quarters, having fewer quarters may pose compliance problems for the state. As appropriate, Region III will coordinate with the states regarding the timing of grant awards.

Reporting

Section 1452(g)(4) of SDWA requires the state to submit a biennial report on the activities allowed under section 1452. The state must report on both the set-aside and project activities in the biennial report [section 35.3570(a)]. In many instances, these two areas are handled by different groups within the state agency and, in some instances, in separate agencies. It is the responsibility of the grantee to assure that all pertinent information is obtained in a timely manner. States should submit their DWSRF biennial/annual reports no later than 90 days after the end of the state fiscal year. At their option, states may choose to submit the reports annually in order to condense the reporting period.

In addition to describing the responsibilities under the DWSRF program of the state agency and EPA, the state's Memorandum of Understanding (MOU) should also discuss responsibilities of each of the groups within an agency and of each department. The directors of the state drinking water programs have agreed to report to Region III on the programmatic aspects of the set-aside activities on a semi-annual basis with the PWSS reporting. Region III will accept these semi-annual reports as meeting the biennial report requirements for the programmatic aspects of the set-aside activities. The state may reference these semi-annual reports in the biennial report. The financial and grants administration aspects of the set-asides activities should be reported in the DWSRF biennial report along with the financial information on the other portions of the DWSRF program. Region III is developing separate guidance on reporting of set-aside activities. It will be provided to the states for review when available. That guidance will discuss the scheduling and coordination of various drinking water program reporting requirements.

The biennial reports, or in some instances, annual reports, will be reviewed prior to Region III's annual on-site visit to the state. Although the reports are required to be submitted every two years, EPA will be conducting on-site review visits annually. In those years that states do not submit biennial reports, Region III will review data from the Drinking Water National Information Management System (DWNIMS). States are required to report data annually to DWNIMS [section 35.3570(d)]. Region III will minimize its request for information in addition to that in DWNIMS.

APPENDICES

CAPACITY DEVELOPMENT STRATEGY FOR EXISTING SYSTEMS FACT SHEET

Requirements:

- Section 1420(c) -- Existing Systems:

The state must develop and implement a strategy to assist PWSs in acquiring and maintaining technical, managerial, and financial capacity.

Section 1420(c)(2) -- *"... In preparing their capacity development strategies, the state must consider, solicit public comment on, and include as appropriate--*

- A. *The methods or criteria that the state will use to identify and prioritize the PWSs most in need of improving technical, managerial, and financial capacity.*
- B. *A description of the institutional, regulatory, financial, tax, or legal factors at the Federal, state, or local level that encourage or impair capacity development.*
- C. *A description of how the state will use the authorities and resources of this title or other means to -*
 - I. *Assist public water systems in complying with NPDWRs;*
 - II. *Encourage the development of partnerships between public water systems to enhance the technical, managerial, and financial capacity of the systems; and*
 - III. *Assist public water systems in the training and certification of operators.*
- D. *A description of how the state will establish a baseline and measure improvements in capacity with respect to NPDWRs and state drinking water law.*
- E. *An identification of the persons that have an interest in and are involved in the development and implementation of the capacity development strategy (including all appropriate agencies of Federal, state, and local governments, private and nonprofit PWSs and PWS customers)."*

- Section 1452(a)(3) -- SRF Applicants:
No assistance shall be provided to a public water system that *"...does not have the technical, managerial, and financial capability to ensure compliance with requirements of this title..."*
- Section 1452(c) -- Withholding:
"(1) In general.--Beginning 4 years after the date of enactment of this section, a state shall receive only--
(A) 90 percent in fiscal year 2001;
(B) 85 percent in fiscal year 2002; and
(C) 80 percent in each subsequent fiscal year, of the allotment that the state is otherwise entitled to receive under section 1452 (relating to state loan funds), unless the state is developing and implementing a strategy to assist public water systems in acquiring and maintaining technical, managerial, and financial capacity."
(D) The maximum that will be withheld if a state fails to meet the requirements of both the capacity development strategy and new system authority provisions is 20% in any fiscal year.

Dates:

- For fiscal year 2001, the withholding determination will be based on the program status as of October 1, 2000. The withholding (10%) will apply to the fiscal year 2001 allotment. Unobligated funds from previous fiscal years will not be subject to withholding.
- For fiscal year 2002, the withholding determination will be based on the program status as of October 1, 2001. The withholding (15%) will apply to the fiscal year 2002 allotment.
- For fiscal year 2003 and beyond, the withholding determination will be based on the program status as of October 1 of the fiscal year. The withholding (20%) will apply to the fiscal year allotment.

What:

The state must document that it has and is implementing a capacity development strategy for existing systems. The documentation must include:

- The state must certify that it solicited public comments on the five elements (A-E) listed above as part of the preparation of its capacity development strategy. The state must describe relevant public comments and its responses to them.
- The state must describe which of the listed elements (A-E) the state has included or excluded from its strategy, and why each element was included or excluded.

- The state must describe how the selected elements together can be rationally considered to constitute a strategy to assist PWSs in acquiring and maintaining technical, managerial, and financial capacity.
- The state must describe how it will implement its strategy and evaluate its progress toward improving PWS capacity.

Capacity Development Strategy Implementation:

- Each year, as a stand-alone submittal or as part of the state's capitalization grant application, the state must provide documentation showing the ongoing implementation of their capacity development strategy.
- Such documentation may consist of a concise narrative description of the major activities being conducted and planned for under the states capacity development strategy.

Annual Review and Ongoing Reporting Requirements:

- By August 6, 2000 and every 3 years thereafter, the state must submit to EPA a list of community water systems and nontransient non-community water systems that have a history of significant noncompliance and, to the extent practicable, the reasons for their noncompliance.
- By August 6, 2001 the state must report to EPA on the success of its enforcement mechanisms and initial capacity development efforts in helping CWSs and NTNCWSs having a history of significant noncompliance improve their capacity.
- Not later than 2 years after a state adopts a capacity development strategy, and every 3 years thereafter, the primacy agency must submit a report to the Governor on the efficacy of the strategy and progress made toward improving the technical, managerial, and financial capacity of PWSs in the state. The report shall also be made available to the public.

CAPACITY DEVELOPMENT AUTHORITY (NEW SYSTEMS) Program Implementation and Annual Review

In the fiscal years following a state's initial documentation of a fully functional program, a state must document that it is requiring a demonstration of technical, managerial, and financial capacity by every new CWS and every new NTNCWS. This documentation of ongoing implementation of the new systems program may be included with a given year's capitalization grant application or it may be provided in an entirely separate submittal. Documentation could consist of summary statistics regarding the number of proposed new CWSs and NTNCWSs and the results of their required capacity demonstrations. The documentation should address methods used to evaluate and verify program implementation.

Each progress report (mid-year and end-of-year) should include:

- Number and list of proposed new CWSs and NTNCWSs
- Number and list of approved new CWSs and NTNCWSs
- Number and list of new CWSs and NTNCWSs (commencing operation after October 1, 1999) that are not in compliance

Below is a table that could be used to report data on the implementation of the program.

Progress Report	
Reporting Period: _____	
Number of proposed new CWSs	
Number of proposed new NTNCWSs	
Number of approved new CWSs	
Number of approved new NTNCWSs	
Number of new CWSs (commenced operation after October 1, 1999)	
Number of new NTNCWSs (commenced operation after October 1, 1999)	
Number of new CWSs that are not in compliance	
Number of new NTNCWSs that are not in compliance	

Any changes to the state's legal authority or other means to ensure the technical, managerial, and financial capacity of new CWSs and NTNCWSs must be reported to U.S. EPA Region III with explanation if the changes affect the state's implementation of

the program. An Attorney General statement may be needed. The program will be evaluated as of October 1 of each year. Failure to demonstrate full, ongoing implementation of its new systems program **each year**, will result in 20% withholding of the state's SRF grant. The maximum that will be withheld if a state fails to meet the requirements of both the capacity development strategy and new system authority provisions is 20% in any fiscal year.

**OPERATOR CERTIFICATION PROGRAM:
POTENTIAL WITHHOLDING**

To be provided. Procedures currently under development.

The proposal was outlined in the Federal Register notice dated July 20, 2000.

This section will be provided when available at a later date.

EXAMPLE APPLICATION MATERIALS

- Pennsylvania DWSRF SF 424 and 424A (Budget Information)
- Pennsylvania DWSRF Intended Use Plan – Financial Charts
- Pennsylvania DWSRF Intended Use Plan – Project Descriptions

F:\USER\SHARE\srf\guidance\6iupguid.wpd